

September 19, 2016



**Clerk of the Board**

**Sent via Electronic Submittal**

Mr. Richard Corey, Executive Officer  
California Air Resources Board  
1001 I Street  
Sacramento, CA 95814

Dear Mr. Corey:

The State Water Contractors (SWC) submits these comments on the California Air Resources Board (CARB) Proposed Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms ("Proposed Amendments"), released August 2, 2016.

These comments continue the dialogue with CARB dating to our January 11, 2010 letter to ARB (attached), the SWC June 3, 2011 letter to ARB (attached), the Air Resources Board Resolution 11-32 and Mary Nichols August 27, 2012 Letter to Jeff Kightlinger, General Manager Metropolitan Water District of Southern California (attached). The purpose of these communications is to mitigate the cost burden the ARB Cap-and-Trade program imposes on the customers of the State Water Project

## **Background**

The State Water Contractors is a non-profit, mutual benefit corporation organized under the laws of the State of California, comprised of 27 public agencies holding contracts to purchase water delivered by the State Water Resources Development System, otherwise known as the State Water Project ("SWP"), which is owned and operated by the California Department of Water Resources ("DWR"). SWC's public agency members are the beneficial users of the SWP, providing water for drinking, commercial, industrial, and agricultural purposes to a population of more than 20 million people and to over 750,000 acres of farmland throughout the San Francisco Bay Area, the Central Valley of California, and Southern California. The primary purpose of the SWP is to store and deliver water to the customers of the SWP, who pay all of its costs. A significant part of the SWP costs relate to water generated and purchased at wholesale for the ultimate purpose of pumping water to consumers across wide areas of the State.

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Delivery of this water is vital to the health, welfare, and productivity of the State of California. Implementing AB 32, SB 350 and SB 32 measures is having a significant impact on the SWP customers. That is true even though the SWP relies on a power supply that is more than 60 percent carbon free. Thus, the SWC has a vested interest in the ongoing development of the Proposed Amendments.

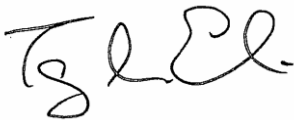
In our communications with ARB we have pointed out the inequitable treatment of the SWP customers in comparison to others that are similarly situated. That inequity leads to the SWP customers being exposed to the risk of “skyrocketing prices” when the economy experiences robust growth<sup>1</sup>. But even during periods of stagnant to moderate growth, the SWP customer’s Cap-and-Trade cost burden has been significant. The Board directed the inequity be addressed in its Resolution 11-32. Chairman Nichols’ 2012 letter set forth a temporary path to partial relief. However, questions about the future viability of the Cap-and-Trade program and evolving priorities of the Investment Plan show that is not a sustainable solution.

## **Conclusion**

The SWC encourage the ARB to take this opportunity allocate emission allowances to the SWP in a fashion similar to the electric utilities. This will address the oversight that has led to the inequitable treatment of the SWP customers, mitigate significant costs and risk of skyrocketing prices and provide a sustainable path forward that is under the control of ARB.

Tim Haines will contact Executive Officer Richard Corey to discuss this opportunity further.

Sincerely,

A handwritten signature in black ink, appearing to read "T. Erlewine", with a stylized, cursive script.

Terry Erlewine  
General Manager

Attachments:

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<sup>1</sup> Severin Borenstein, Fixing a Major Flaw in Cap-and-Trade, <https://energyathaas.wordpress.com/2016/08/15/fixing-a-major-flaw-in-cap-and-trade/>

January 11, 2010

Mr. Kevin Kennedy, Ph.D.  
Assistant Executive Officer  
Office of Climate Change  
California Air Resources Board  
1001 I Street  
Sacramento, CA 94814

**Re: California Air Resources Board's "Preliminary Draft Regulation for a California Cap-and-Trade Program"**

Dear Mr. Kennedy:

The State Water Contractors (SWC) thank the California Air Resources Board (ARB) for seeking comments on the "Preliminary Draft Regulations for the Cap-and-Trade Program" (Proposed Regulations). The SWC<sup>1</sup> is a non-profit, mutual benefit corporation organized under the laws of the State of California, comprised of 27 public agencies holding contracts to purchase water delivered by the State Water Resources Development System, otherwise known as the State Water Project (SWP), which is owned and operated by the California Department of Water Resources (DWR). SWC's public agency members are the beneficial users of the SWP, which provides water for drinking, commercial, industrial, and agricultural purposes to a population of more than 25 million people and to over 750,000 acres of farmland throughout the San Francisco Bay-Area, the Central Valley of California, and Southern California. The primary purpose of the SWP is to store and deliver water to the SWP contractors, who pay all of the costs incurred by the SWP.

DWR manages a power resource portfolio solely for the purpose of delivering water to SWP contractors. There are no electricity customers served by the SWP. The SWP contractors' ability to reliably and economically serve their customers is in jeopardy due to reduced snowpack, prolonged drought and



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Terry Erlewine

<sup>1</sup>The SWC members are: Alameda County Flood Control & Water Conservation District, Zone 7; Alameda County Water District; Antelope Valley-East Kern Water Agency; Casitas Municipal Water District on behalf of the Ventura County Flood Control District; Castaic Lake Water Agency; Central Coast Water Authority on behalf of the Santa Barbara County Flood Control & Water Conservation District; City of Yuba City; Coachella Valley Water District; County of Kings; Crestline-Lake Arrowhead Water Agency; Desert Water Agency; Dudley Ridge Water District; Empire-West Side Irrigation District; Kern County Water Agency; Littlerock Creek Irrigation District; The Metropolitan Water District of Southern California; Mojave Water Agency; Napa County Flood Control & Water Conservation District; Oak Flat Water District; Palmdale Water District; San Bernardino Valley Municipal Water District; San Gabriel Valley Municipal Water District; San Geronio Pass Water Agency; San Luis Obispo Co. Flood Control & Water Conservation District; Santa Clara Valley Water District; Solano County Water Agency; and Tulare Lake Basin Water Storage District.

other conditions attributed to GHG. That is why the SWC have supported the efforts of DWR to reduce carbon emissions. More than 50% of the energy used to deliver water is produced from clean, carbon free hydroelectric generation. With the support of the SWP contractors, DWR has already taken steps to significantly reduce the SWP carbon footprint. That action will reduce SWP GHG emissions below 1990 levels and will provide a significant contribution toward achieving California's AB32 goals. The SWP contractors further support a DWR emission reduction policy that combines additional renewable energy and energy efficiency to achieve further GHG reductions. We view the Proposed Regulation program as complementary to the measures DWR has already initiated to reduce SWP GHG emissions. However, we are concerned that, as proposed, the program will create inequities and have unintended consequences.

ARB's consultants, the Economic and Allocation Advisory Committee (EAAC), estimate the value of the emission allowances at between \$2.5 billion to 7.5 billion in 2012. EAAC expects those cost to increase to between \$7.5 billion and \$22 billion in 2020.<sup>2</sup> These estimates are based on an EAAC assumption that all emission allowances are auctioned. The SWC suggests instead that ARB provide free allowances to carbon emitters and auction only those allowances needed to fund "Additional Reductions Necessary to Achieve the Cap." This approach reduces to 34.4 MMTCO<sub>2</sub> of emission allowances auctioned in 2020 instead of 365 MMTCO<sub>2</sub> assumed by EAAC.<sup>3</sup> Limiting the number of allowances auctioned will help avoid the significant inequities that will likely be imposed on the SWP customers by the Proposed Regulation. Alternatively, the proposal by the Joint Utilities may also help avoid inequities, if it is properly structured and allocates allowances to all covered entities having a surrender obligation for electricity used to serve electric and water customers.<sup>4</sup> However even a modified Joint Utilities proposal will lead to unintended consequences because of the amount of dollars this program will collect and redistribute.

To underscore our concern regarding unintended consequences of the Proposed Regulation we refer ARB to the effort to redesign the California electricity markets. That effort was born of good intentions, involved the allocation of a scarce resource through an auction, and transferred significant dollars between participants. In 2000 and 2001, "California was rocked by energy shortages and skyrocketing electricity prices."<sup>5</sup> State and federal policy makers and regulators were ill-equipped to deal with manipulation of the poor market design. Our first lesson from that catastrophe is "policy makers must respect market forces."<sup>6</sup> The customers of the SWP continue to pay for the unintended consequences of the attempt to restructure the California electricity market. The SWC is disturbed to find minimal consideration in the tone or substance of the

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<sup>2</sup> Recommendations to the California Air Resources Board from the Economic and Allocation Advisory. Untitled Table 3, "Allocating Emissions Allowances Under California's Cap-and-Trade Program."

<[http://climatechange.ca.gov/eaac/documents/eaac\\_reports/2010-01-07\\_EAAC\\_Allocation\\_Report\\_Draft.pdf](http://climatechange.ca.gov/eaac/documents/eaac_reports/2010-01-07_EAAC_Allocation_Report_Draft.pdf)> (January 7, 2010)

<sup>3</sup> California Air Resources Board. Table 2: Recommended Greenhouse Gas Reduction Measures, "Climate Change Scoping Plan."

<<http://www.arb.ca.gov/cc/scopingplan/document/scopingplandocument.htm>>. (December 2008)

<sup>4</sup> THE JOINT UTILITIES. Letter to EAAC. January 6, 2010.

<sup>5</sup> Susan P. Kennedy. "The Oh Decade: California's electricity crisis stung – but made us stronger." Special to The Sacramento Bee. January 1, 2010.

<sup>6</sup> *ibid*

Proposed Regulation that ARB will apply the lessons learned from the California Electricity Crisis.

Another aspect of the Proposed Regulation that will lead to unintended consequences is that it permits parties that do not have surrender obligations to “opt in” to the auction process. Such parties will participate in the auction solely for their financial gain. These speculators will increase the volatility of the price of emissions, bid up the price of allowances and create the highest possible cost for those with a surrender obligation. Allowing speculators to opt-in that have no vested interest in containing the cost of emissions will likely lead to higher costs to California’s families and businesses and achieve no reduction in GHG emissions.

As currently contemplated, the Cap-and-Trade program will have a far greater impact on the California economy and the costs to the SWP customers than we had expected. Our comments are intended to avoid the inequities and unintended consequences that the Proposed Regulation will likely create. The SWC appreciates this opportunity to comment on the Proposed Regulation. We look forward to meeting with ARB staff if you would like to discuss our comments.

Sincerely,

A handwritten signature in dark ink, appearing to read "T Erlewine". The signature is fluid and cursive, with the first letter of the last name being a large, stylized 'E'.

Terry Erlewine  
General Manager



June 3, 2011

Mr. James Goldstene  
Executive Officer  
California Air Resources Board  
P.O. Box 2815  
Sacramento, CA 95812

Dear Mr. Goldstene:

The State Water Contractors is a non-profit, mutual benefit corporation organized under the laws of the State of California, comprised of 27 public agencies holding contracts to purchase water delivered by the State Water Resources Development System, otherwise known as the State Water Project ("SWP"), which is owned and operated by the California Department of Water Resources ("DWR"). SWC's public agency members are the beneficial users of the SWP, providing water for drinking, commercial, industrial, and agricultural purposes to a population of more than 25 million people and to over 750,000 acres of farmland throughout the San Francisco Bay Area, the Central Valley of California, and Southern California. The primary purpose of the SWP is to store and deliver water to the customers of the SWP, who pay all of its costs. A significant part of the SWP costs relate to water generated and purchased at wholesale for the ultimate purpose of pumping water to consumers across wide areas of the State.

Delivery of this water is vital to the health, welfare, and productivity of the State of California. Pumping required to deliver those very critical SWP supplies consumes an average of about 4,000 gigawatt-hours annually more than is generated from its hydropower operations – or about 4 percent of the state-wide use of electricity. Implementing AB 32 measures will have a significant impact on the State's water customers. Thus, the SWC has a vested interest in the ongoing development of regulations for implementing AB 32. We – along with DWR staff – have been active participants in the development of the Cap and Trade regulations. It was in response to our comments that Assistant Executive Officer Kevin Kennedy acknowledged to the Board that staff had overlooked cost impacts to the customers of the SWP. Mr. Kennedy gave assurances to the Board that he would investigate how the SWP customers could receive treatment similar to that being applied to the customers of the electric distribution customers in a discussion leading to the Board adopting the regulations.

Unfortunately, we are no closer to achieving that outcome nearly six months later. The SWP emission allowances continue to be allocated to the electric distributions utilities instead of to the water agencies. It is unlikely the Board or Mr. Kennedy intended that the water customers would subsidize the electric customers in this fashion. Furthermore, we do not believe it was the Board's intent that the water customers enter this transition period being singularly



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Mr. James Goldstene

June 3, 2011

Page 2

exposed to the rate increases inherent to untested markets. It should be also noted that the price signals that are so vital to modifying the behavior of customers are lost to the water customers if this oversight continues.

During the course of the Board hearing Mr. Kennedy indicated to the Board and customers of the State Water Project that water customers could receive free allowances to mitigate price increases. It seems that this has been forgotten with Mr. Kennedy's departure. We would like to meet with you in order to explore ways to put this back on the track contemplated by Mr. Kennedy and the Board. Please contact me at 916-447-7357 (x203) or Tim Haines (x205).

Sincerely Yours,

A handwritten signature in dark ink, appearing to read 'TLE', with a stylized flourish at the end.

Terry L. Erlewine  
General Manager



# Air Resources Board



**Matthew Rodriguez**  
Secretary for  
Environmental Protection

**Mary D. Nichols, Chairman**  
1001 I Street • P.O. Box 2815  
Sacramento, California 95812 • [www.arb.ca.gov](http://www.arb.ca.gov)

**Edmund G. Brown Jr.**  
Governor

August 27, 2012

Mr. Jeff Kightlinger, General Manager  
Metropolitan Water District of Southern California  
700 North Alameda Street  
Los Angeles, CA 90012-2944

Dear Jeff:

As you know, water use in California is extremely energy intensive resulting in significant greenhouse emissions. Water-related energy use consumes nearly 20 percent of our annual electricity and close to 30 percent of our natural gas.

California's AB 32 Climate Change Scoping Plan highlights the importance of taking steps to improve water efficiency and conservation as a key part of the state's plan to cut greenhouse gas emissions. Additionally, as the *Economic and Technology Advancement Advisory Committee* for AB 32 points out, policies and technologies that increase the efficiency of the state's water delivery systems and reduce end-use will produce multiple environmental and economic benefits.

As we have discussed, the state is developing an investment plan for the use of funds from the auction of allowances under the cap and trade program to further the purposes of AB 32. As part of this process, ARB is fully committed to working with Metropolitan Water District and the State Water Project to develop and implement a plan that will provide funds for investment in water efficiency and conservation projects that reduce greenhouse gas emissions.

This approach will ensure that you are able to cost-effectively comply with the cap and trade program and continue taking actions that will provide long-term economic and environmental benefits for California.

We look forward to working with you in this effort.

Sincerely,

Mary D. Nichols  
Chairman

*The energy challenge facing California is real. Every Californian needs to take immediate action to reduce energy consumption.  
For a list of simple ways you can reduce demand and cut your energy costs, see our website: <http://www.arb.ca.gov>.*

California Environmental Protection Agency